

## Financial Services Committee, Subcommittee on Oversight and Investigations Hearing 4/28/21 | Written Testimony of Chelsea McDaniel

Good afternoon Chairwoman Waters, Ranking Member McHenry and members of the Subcommittee. Thank you for the opportunity to appear before you today to discuss the Role of Municipal Bond Markets in Advancing – and Undermining – Economic, Racial and Social Justice.

I am Chelsea McDaniel (*she/her/hers*) and I am a Senior Fellow at Activest. Activest is an investment research firm that quantifies fiscal justice risk within the municipal bond market. We define Fiscal Justice as the analysis of public budgets at the intersection of fiscal health and racial justice. Our thesis is simple: communities and public entities that treat their residents and clients more justly realize stronger fiscal outcomes over the intermediate and long term. We are not only critics of the market but also market participants, through efforts like the Fiscal Justice Municipal Investment Strategies we develop alongside groups like Asasina Social Capital, or the Fiscal Justice Credit Rating Agency we're launching this year. Our work blends economic modeling, financial analysis, and social policy research, and we exist to protect savers and everyday municipal investors from taking on hidden and uncompensated risks of the more egregiously unjust corners of the municipal market.

Today I'd like to present a high level sectoral view of postsecondary education institutions, in the context of the larger municipal finance market.

Broadly, we've seen that social and environmental risks have emerged within public entities, like local governments and schools, as a result of longstanding policies born out of segregation era views of development and progress that have yet to be updated.

Whether it's the \$70 billion in municipal revenue that schools lose annually to corporate tax incentives, the \$11 billion lost to exclusionary school discipline policies, the \$2 billion for municipal settlements, or the \$7 billion of excessive fines and fees disproportionately extracted from BIPOC communities, inequitable public budget serve as the supply lines to fueling state-sanctioned, taxpayer-funded exclusion and oppression. U.S. local government finance is built on a long history of sordid financial practices, and the current public finance system does a poor job of integrating the social and fiscal cost of racial equity into the evaluation of cities and bond issuances.

This sordid history stretch back to 1827, when Louisiana used its "full faith and credit" to back a series of bank bonds whose proceeds were used to purchase slaves, and extends through today, when cities like Kenosha, WI give away 20% of its budget in tax incentives but argue that there's not enough money to purchase the body cameras that may have held Jacob Blake's shooter accountable.

The fiscal and budgetary cost of ignoring the fiscal justice risks is growing as the reported incidence and pricing severity of fiscal justice events are growing within government

entities, including postsecondary institutions. In the world of postsecondary finance, Activest's research has focused on the ways in which PWIs, Predominantly White Institutions, have been extractive as opposed to collaborative, let alone peacefully coexisting, with MSIs (Minority Serving Institutions). Although PWIs' fiscal justice risks have been unpriced in the past, their materiality is growing in realtime, and the long-tail risk of their prior behavior is likewise expanding.

Three examples of this growing materiality include predatory inclusion in higher education loans, which scholar Louise Seamster defines as the process where student loan companies offer needed services to students of color on exploitative terms that limit or eliminate their long-term benefits; the outsized pricing among HBCU bonds, evidenced by Chris Parson's study on Racial discrimination in higher education bond markets; and third, postsecondary schools racing to become federally recognized HSIs to capitalize off of the growing Latinx student population, where scholar Gina Garcia discusses what it means to move from simply *enrolling* Latinx students to actually *servicing* them.

From a credit perspective, we see MSIs as strong municipal investments, as opposed to PWIs, which are evidencing a growing body of unpriced fiscal justice risks. Accordingly, we've developed a series of recommendations to counter the aforementioned fiscal justice risks in the postsecondary market.

### **1. Accounting for Equity Research**

First, we see a need for a study to track and quantify all of the federal and state funding withheld from MSIs since their inception, and the estimated financial impact on states and the federal government when these payments come due. This research has been partially completed for TCUs through efforts like the Land Grab Universities project, but more research remains for HBCUs, PBIs, and HSIs. We anticipate at least two components. The first component focuses on long-term liabilities, which would be a historical account of the financial support that was denied and stolen from MSIs since their creation. The second component would be an examination of current liabilities, which is an investigation of the current cases for fair funding and a new equation for evaluating the overall investment in MSIs.

### **2. Social Justice Bonds**

A bond offering that seeks to correct for past wrongs for all eligible HBCUs and TCUs. For HBCUs, it mirrors the size of each schools' initial land grant. The reparations bond would be of an unprecedented size to meet an unprecedented need.

- The structure of the bond would be a \$4 billion zero coupon, zero-interest bond open to individual investors in small denominations of \$500 or more.
- The use of proceeds includes capital improvements typical of bond offerings, as well as bond refinancing.
- Ten percent of the principal would be forgiven and funded by philanthropic dollars.
- The amount of the bond reflects the total size of the HBCU capital finance program (\$1.8 billion outstanding as of 2017) plus an additional 2 to 3 billion for the 50 HBCUs that

don't currently participate in the program. The bonds would be repaid with future tuition proceeds that would result from schools' expanded student capacity.

### **3. Investment in Physical Assets**

"We're called 'Historic' because that was the last time there was a significant investment made into our physical infrastructure." - HBCU President

Property is often the only endowment of many MSIs. Through prominent inclusion in the infrastructure package and publicly supported bonds to help finance this effort, there is an opportunity to support MSIs in strengthening their financial health through the acquisition and development of their physical assets. MSIs are often anchor institutions in their communities and are regularly some of the largest land and property owners. There are several benefits to these institutions owning and professionally managing their land and property:

- Substantial economic spillover driven through asset expansion and community development.
- Underutilized assets (informal endowments) that can generate institutional revenue at relatively low carrying and borrowing costs.
- Maintenance of culturally and historically-relevant assets with approx 11% of HBCU buildings being historic, high-maintenance, but also, tax-credit eligible institutions.

Again, we thank you for your time and the opportunity to present our investment research and thesis to the subcommittee.